Supreme Court, U.S.
FILED
DEC 3 1985
JOSEPH F. SPANIOL, JR.
CLERK

Nos. 85-558, 85-559 and 85-560

In the Supreme Court of the United States

OCTOBER TERM, 1985

ROBERT E. O'CONNOR AND GLADYS E. O'CONNOR,
PETITIONERS

v.

UNITED STATES OF AMERICA

PAUL H. COPLIN AND PATRICIA COPLIN, PETITIONERS

v.

UNITED STATES OF AMERICA

JACK R. MATTOX AND MARIA MATTOX, PETITIONERS

v.

UNITED STATES OF AMERICA

ON PETITIONS FOR A WRIT OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE FEDERAL CIRCUIT

BRIEF FOR THE UNITED STATES

CHARLES FRIED
Solicitor General

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QUESTION PRESENTED

Whether the court below correctly determined that Article XV of the Agreement in Implementation of Article III of the Panama Canal Treaty, Sept. 7, 1977, United States-Panama, T.I.A.S. No. 10031, did not exempt the petitioners from United States taxation on the salaries that they received from the Panama Canal Commission.

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Treaty, executive agreement, and statute:

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Agreement in Implementation of Article III of the Panama Canal Treaty, Sept. 7, 1977, United States-Panama, T.I.A.S. No. 10031:
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OCTOBER TERM, 1985

No. 85-558

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ON PETITIONS FOR A WRIT OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE FEDERAL CIRCUIT

BRIEF FOR THE UNITED STATES

OPINIONS BELOW

The opinion of the court of appeals (Pet. App. 1a-8a) is reported at 761 F.2d 688. The opinion of the United States Claims Court (Pet. App. 9a-69a) is reported at 6 Cl. Ct. 115.

JURISDICTION

The judgments of the court of appeals were entered on May 10, 1985, and petitions for rehearing were denied on July 3, 1985 (Pet. App. 70a-71a). The petitions for a writ of certiorari were filed on September 30, 1985. The jurisdiction of this Court is invoked under 28 U.S.C. 1254(1).

TREATY AND EXECUTIVE AGREEMENT INVOLVED

Article III, paragraph 9, of the Panama Canal Treaty, Sept. 7, 1977, United States-Panama, T.I.A.S. No. 10030, and Article XV of the Agreement in Implementation of Article III of the Panama Canal Treaty, T.I.A.S. No. 10031, are set forth in App. A, *infra*.

STATEMENT

1. On September 7, 1977, the United States and the Republic of Panama signed the Panama Canal Treaty, which was approved by the Senate and entered into force on October 1, 1979. That treaty restored to Panama territorial sovereignty over the Canal Zone, while granting to the United States the right to manage, operate and maintain the canal until the year 2000 under the auspices of the Panama Canal Commission (Commission), an agency of the United States government (Pet. App. 3a). Article III, paragraph 9, of the treaty provides in pertinent part that "the rights and legal status of United

States Government agencies and employees operating in the Republic of Panama pursuant to this Article, shall be governed by the Agreement in Implementation of this Article, signed this date." Article XV of the Agreement in Implementation of Article III of the Panama Canal Treaty, also signed on September 7, 1977, provides in pertinent part as follows:

Taxation

> 1. By virtue of this Agreement, the Commission, its contractors and subcontractors, are exempt from payment in the Republic of Panama of all taxes, fees or other charges on their activities or property.
>
> 2. United States citizen employees and dependents shall be exempt from any taxes, fees, or other charges on income received as a result of their work for the Commission. Similarly, they shall be exempt from payment of taxes, fees or other charges on income derived from sources outside the Republic of Panama.
>
> 3. United States citizen employees and dependents shall be exempt from taxes, fees, or other charges on gifts or inheritance or on personal property, the presence of which within the territory of the Republic of Panama is due solely to the stay therein of such persons on account of their or their sponsor's work with the Commission.

2. Petitioners Robert O'Connor, Paul Coplin and Jack Mattox are United States citizens who were employed by the Commission during the relevant tax years.[1] The wages they received from the Commission

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[1] Gladys E. O'Connor, Patricia Coplin and Maria R. Mattox are parties to these suits because each filed a joint tax return with her husband. Unless otherwise stated, we will refer to Robert O'Connor, Paul Coplin and Jack Mattox as petitioners.

were included in computing their federal income tax for years 1979 (Coplin), 1980 (Mattox) and 1981 (O'Connor and Mattox). Thereafter, petitioners filed claims for refund for the amount of tax paid with respect to income received from the Commission, urging that Article XV of the Agreement in Implementation of Article III of the Panama Canal Treaty exempted that income from domestic taxation. The Internal Revenue Service denied each of their claims, and each petitioner filed a suit for refund in the Claims Court (Pet. App. 2a).

The Claims Court rejected the government's argument that Article XV of the Implementation Agreement was not intended to restrict the right of the United States to tax its citizens. The Claims Court also determined that, even though the Executive Branch had consistently interpreted the Agreement as implicating only Panamanian taxes, a broad, literal interpretation of the Implementation Agreement was required because the government presented "*no evidence whatsoever* as to the interpretation given this language by Panama" (Pet. App. 3a, 29a, 61a-66a, 68a-69a (emphasis in original)).

3. On appeal, the Federal Circuit unanimously reversed. Shortly before oral argument in the court of appeals, the Foreign Minister of the Republic of Panama delivered to the United States government a diplomatic note confirming that the Foreign Ministry of Panama agreed with the United States that Article XV of the Implementation Agreement was not intended to affect United States taxation of Commission employees (App. B, *infra*, 4a-9a; Pet. App. 5a). The Federal Circuit denied petitioners' motion to strike the Panamanian government's note and, con-

sistent with decisions of this Court, considered the views of the Panamanian government. The court stated (Pet. App. 6a) that its role in treaty matters was limited "'to giving effect to the intent of the Treaty parties.'" Since the treaty partners agreed that Article XV of the Implementation Agreement did not exempt the salaries paid to the Commission's United States citizen employees from domestic taxation, the trial court's contrary determination was reversed (Pet. App. 6a-7a). In a concurring opinion, three members of the five judge panel concluded (Pet. App. 8a) that "[a] complete reading of the record [before the Claims Court], the treaty and the Implementation Agreement" indicated that Article XV had no bearing on the power of the United States to tax its own citizens and that it was not necessary to consider the note from the Panamanian government to reach that result.

DISCUSSION

The decision below correctly held that Article XV of the Implementation Agreement did not exempt United States citizens from United States taxation on salaries paid by the Commission.

1. The world-wide income of United States citizens is subject to taxation by the United States regardless of the citizen's residence or the source of such income. Section 1, Internal Revenue Code of 1954 (26 U.S.C.); *Cook* v. *Tait*, 265 U.S. 47, 56 (1924). As has long been recognized, exemption from taxation is a matter of legislative grace and must be granted explicitly. *HCSC-Laundry* v. *United States*, 450 U.S. 1, 5 (1981); *Commissioner* v. *Glenshaw Glass Co.*, 348 U.S. 426, 429-430 (1955); *Helvering* v. *Northwest Steel Rolling Mills, Inc.*, 311 U.S. 46,

49 (1940); *United States Trust Co.* v. *Helvering*, 307 U.S. 57, 60 (1939). There is no merit to petitioners' claim that Article XV constitutes such an express exemption, permitting them to avoid all taxation on the salaries received from the Commission.

As this Court has indicated, the role of a court in interpreting international agreements is "limited to giving effect to the intent of the Treaty parties." *Sumitomo Shoji America, Inc.* v. *Avagliano*, 457 U.S. 176, 185 (1982). See also *In re Ross*, 140 U.S. 453, 475 (1891). In determining that intent, the courts appropriately examine not only the language used in the treaty, but also the context in which the language is used, the history of negotiations underlying the agreement and the proceedings before the Senate. See *Sumitomo Shoji America, Inc.* v. *Avagliano*, 457 U.S. at 180; *Factor* v. *Laubenheimer*, 290 U.S. 276, 294-295 (1933); *Nielsen* v. *Johnson*, 279 U.S. 47, 52 (1929). Indeed, this Court has not confined its search for guides to the intent of the parties to documents presented to lower courts, but has examined records and expressions of intent of a foreign government that were presented to it for the first time. *Sumitomo Shoji America, Inc.* v. *Avagliano*, 457 U.S. at 184, n.9; *Factor* v. *Laubenheimer*, 290 U.S. at 295 (this Court's order for reargument invited counsel to conduct a further search through available diplomatic records and correspondence); *United States* v. *Reynes*, 50 U.S. (9 How.) 127, 147-148 (1850).

While the ultimate goal of adjudication is to effect the treaty partners' intent, it has long been settled that the construction of an international agreement by the Executive Branch is entitled to great deference by the courts. *Sumitomo Shoji America, Inc.* v. *Avagliano*, 457 U.S. at 180-184; *Factor* v. *Lauben-*

heimer, 290 U.S. at 295. It is, after all, the Executive Branch that is charged with conducting foreign affairs. For that reason, deference is the rule even when the treaty partner takes a view different from that taken by the United States. *Factor* v. *Laubenheimer*, 290 U.S. at 298; *Charlton* v. *Kelly*, 229 U.S. 447, 473 (1913); *Whitney* v. *Robertson*, 124 U.S. 190, 194-195 (1888); *United States* v. *A.L. Burbank & Co.*, 525 F.2d 9, 15 (2d Cir. 1975), cert. denied, 426 U.S. 934 (1976). When, however, "the parties to a treaty both agree as to the meaning of a treaty provision, and that interpretation follows from the clear treaty language, we must, absent extraordinarily strong contrary evidence, defer to that interpretation." *Sumitomo Shoji America, Inc.* v. *Avagliano*, *supra*, 457 U.S. at 185. In the present case, the United States has consistently maintained that Article XV of the Implementation Agreement does not exempt from United States taxation the salaries paid to the Commission's United States citizens.

2. An examination of the language of Article XV, the history surrounding its negotiations, and the proceedings leading to Senate ratification of the Treaty underlying the Agreement indicates that it was not intended in any way to restrict the right of the United States to tax its citizens working for the Commission. Paragraph 1 of Article XV exempts the Commission, its contractors and subcontractors from Panamanian taxes. Paragraph 3 of Article XV exempts United States citizen employees of the Commission and their dependents from payment of taxes, fees or other charges on gifts, inheritance and personal property found within the Republic of Panama on account of their own or their sponsor's work for the Panama Canal Commission. Paragraph 2 of that article, which is at issue in this case, provides that

"United States citizen employees and dependents shall be exempt from any taxes, fees, or other charges on income received as a result of their work for the Commission." If there is any doubt that, in context, this refers only to Panamanian tax, that doubt is resolved by the Article's following sentence, which exempts United States citizen employees of the Commission "from payment of taxes, fees or other charges on income derived from sources outside Panama." To read paragraph 2 as petitioners propose would give credence to the argument that even interest earned on United States bank accounts and dividends from domestic corporations are exempt from United States income tax.

Such a result is clearly absurd. Accordingly, even without considering the recent Panamanian diplomatic note, a large majority of courts [2] (and the ma-

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[2] The Tax Court and many district courts have interpreted Article XV, paragraph 2, of the implementing agreement to exempt salaries of United States citizen employees of the Commission from Panamanian income tax, not from United States income tax. *Smith* v. *Commissioner*, 83 T.C. 702 (1984); *McCain* v. *Commissioner*, 81 T.C. 918 (1983); *Bergman* v. *Commissioner*, 50 T.C.M. (CCH) 158 (1985); *Vamprine* v. *Commissioner*, 49 T.C.M. (CCH) 210 (1984), appeal pending, No. 85-4150 (5th Cir.); *Collins* v. *Commissioner*, 47 T.C.M. (CCH) 713 (1983); *Rego* v. *United States*, 591 F. Supp. 123 (W.D. Tenn. 1984); *Stabler* v. *United States*, 84-1 U.S.T.C. para. 9153 (N.D. Tex. Nov. 30, 1983); *Hollowell* v. *United States*, 84-1 U.S.T.C. ¶ 9142 (M.D. Fla. Nov. 21, 1983); *Corliss* v. *United States*, 567 F. Supp. 162 (W.D. Ark. 1983); *Pierpoint* v. *United States*, 83-2 U.S.T.C. ¶ 9647 (S.C. Oct. 3, 1983); *Snider* v. *United States*, 53 A.F.T.R. 2d 349 (W.D. Wash. Sept. 23, 1983); *Stokes* v. *United States*, 83-2 U.S.T.C. ¶ 9644 (W.D. Wash. Aug. 29, 1983). Accord: unreported Western District of Arkansas opinion in *Skrable* v. *United States*, appeal pending No. 85-1743WA (8th Cir.). See also *Billman* v. *Commissioner*, 83 T.C. 534, 541 n.6 (1984). To the

jority of judges on the Federal Circuit panel) has concluded that Article XV focuses exclusively on Panamanian taxation. As those courts have held, the Article's purpose is to extend protections to United States citizen employees of the Commission from taxation by Panama, not to relieve them of their duty to pay United States taxes. This construction is supported by the negotiating history underlying the Treaty and Agreement, which indicates that Panamanian taxes alone were the subject of discussions between the parties. The Legal Adviser of the State Department testified before the Senate Foreign Relations Committee during its considerations of the Panama Canal Treaty that paragraph 2 of Article XV related only to Panamanian taxation, not to United States taxation. *Panama Canal Treaties Before the Senate Comm. on Foreign Relations*, 95th Cong., 1st Sess., Pt. 1, at 268-269 (1977); App. C, *infra*, 10a-12a. The section-by-section analysis of the Treaty and its implementing agreements prepared by the State Department for the United States Senate likewise stated that the Implementing Agreement provided an exemption only from Panamanian taxation. S. Exec. Rep. 95-12, 95th Cong., 2d Sess. 155

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contrary, see *Harris* v. *United States*, 585 F. Supp. 862, 863 (N.D. Ga. 1984), aff'd, 768 F.2d 1240 (11th Cir. 1985). In *Swearingen* v. *United States*, 565 F. Supp. 1019 (Colo. 1983), the court held that an executive agreement, which the Implementation Agreement is, exempting United States citizens from taxation was not within the constitutional powers of the President. In addition, the Tax Court has recently held that in the virtually identical provision of Article XVI of the Agreement in Implementation of Article IV of the Panama Canal Treaty, T.I.A.S. 10032, App. A, *infra* 2a-3a, United States citizen employees of the United States Armed Forces stationed in Panama were not exempt from United States taxation. *Rust* v. *Commissioner*, 85 T.C. No. 15 (Aug. 15, 1985).

(1978). In the introduction to the section-by-section analysis, the Senate Report (*id.* at 127) stated that the analysis was—

> prepared by members of the treaty negotiating team and have been approved by the offices of the State and Defense Departments directly involved in the negotiations * * *. Accordingly, these comments may be considered as an authoritative source of information with respect to the negotiating background and interpretation of the Treaties.

The documentary evidence also reveals that the person who drafted Article XV was likewise one of the drafters of the section-by-section analysis (I C.A. App. 25-26, 46, 64).

3. The foregoing analysis makes clear that, even in the absence of the recent Panamanian diplomatic note, the judgment of the court of appeals is correct. Upon submission of the Panamanian note the point was made conclusively. Even if, as petitioners contend, the language of Article XV suggests a different result, this Court has established that such language does not control if it " 'effects a result inconsistent with the intent or expectations of its signatories.' " *Sumitomo Shoji America, Inc.* v. *Avagliano*, 457 U.S. at 180, quoting *Maximov* v. *United States*, 373 U.S. 49, 54 (1963). Thus, it was entirely correct for the court below to consider the diplomatic note presented to the United States by the Government of the Republic of Panama. Under well-established rules, when both government parties to a bilateral agreement have concurred in its interpretation, it is inappropriate for courts to chart a different course. In discharging its function of treaty interpretation, this Court has consistently turned to authoritative governmental statements, even those made available only late in the

proceedings. *United States* v. *Pink*, 315 U.S. 203, 220-221 (1942). And, once a foreign government presents a statement dealing with matters within its area of sovereign authority, American courts are obligated to accept that statement at face value as "conclusive." *Ibid.*

4. We acknowledge, however, that the decisions of the Federal Circuit conflict with the recent decision of the Eleventh Circuit in *Harris* v. *United States*, 768 F.2d 1240 (1985). In our view, *Harris* fails properly to apply the canons of treaty interpretation set forth by this Court and, in the end, grants an exemption from domestic taxation intended by neither of the treaty partners. Indeed, the Eleventh Circuit's error in disregarding these rules of construction was compounded by its error in refusing to consider the Panamanian diplomatic note because it had not been presented to the lower court. That ruling is directly in conflict not only with the Federal Circuit's contrary ruling in the present cases, but also with the authorities of this Court. *Sumitomo Shoji America, Inc.* v. *Avagliano*, *supra*.

5. As matters now stand, United States citizens who were and are employees of the Commission are subject to different rules of taxation on their salaries from the Commission depending upon where they reside and upon the court in which their claim is heard. The issues presented here are now pending in cases in the Fifth, Eighth, and Eleventh Circuits. We have been informed by the Chief Counsel of the Internal Revenue Service that a recent survey indicates that 1714 cases involving $32,607,000 in tax are either pending administratively or in litigation. The Chief Counsel further informs us that 2000 United States citizens were employed by the Commis-

sion in 1979, 1655 in 1984 and 1360 in 1985. In addition, there are 3890 cases with $13,283,000 in tax involving the exemption of military personnel from taxation under a virtually identical provision in Article XVI(2) of the Agreement in Implementation of Article IV of the Panama Canal Treaty, App. A., *infra*. Given the undisputed conflict of decisions and the administrative importance of the question, we do not oppose the petitions for a writ of certiorari.

CONCLUSION

The petitions for a writ of certiorari should be granted.

Respectfully submitted.

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DECEMBER 1985

APPENDIX A

Panama Canal Treaty Between the United States of America and Panama, Sept. 7, 1977, T.I.A.S. No. 10030:

ARTICLE III

Canal Operation and Management

* * * * *

9. The use of the areas, waters and installations with respect to which the United States of America is granted rights pursuant to this Article, and the rights and legal status of United States Government agencies and employees operating in the Republic of Panama pursuant to this Article, shall be governed by the Agreement in Implementation of this Article, signed this date.

* * * * *

Agreement Between the United States of America and Panama in Implementation of Article III of the Panama Canal Treaty, Sept. 7, 1977, T.I.A.S. No. 10031:

ARTICLE XV

Taxation

1. By virtue of this Agreement, the Commission, its contractors and subcontractors are exempt from payment in the Republic of Panama of all taxes, fees or other charges on their activities or property.

2. United States citizen employees and dependents shall be exempt from any taxes, fees, or

other charges on income received as a result of their work for the Commission. Similarly, they shall be exempt from payment of taxes, fees or other charges on income derived from sources outside the Republic of Panama.

3. United States citizen employees and dependents shall be exempt from taxes, fees, or other charges on gifts or inheritance or on personal property, the presence of which within the territory of the Republic of Panama is due solely to the stay therein of such persons on account of their or their sponsor's work with the Commission.

4. The Coordinating Committee may establish such regulations as may be appropriate for the Implementation of this Article.

Agreement Between the United States of America and Panama in Implementation of Article IV of the Panama Canal Treaty, Sept. 7, 1977, T.I.A.S. No. 10032:

ARTICLE XVI

Taxation

(1) By virtue of this Agreement, the United States Forces are exempt from payment in the Republic of Panama of all taxes, fees or other charges on their activities or property, including those imposed through contractors or subcontractors.

(2) Members of the Forces or the civilian component, and dependents, shall be exempt from any taxes, fees, or other charges on income received as a result of their work for the United

States Forces or for any of the service facilities referred to in Articles XI or XVIII of this Agreement. Similarly, as is provided by Panamanian law, they shall be exempt from payment of taxes, fees or other charges on income derived from sources outside the Republic of Panama.

(3) Members of the Forces or the civilian component, and dependents, shall be exempt from taxes, fees or other charges on gifts or inheritance or on personal property, the presence of which within the territory of the Republic of Panama is due solely to the stay therein of such persons on account of their or their sponsor's work with the United States Forces.

(4) The Joint Committee may establish such regulations as may be appropriate for the implementation of this Article.

APPENDIX B

[Note from Government of the Republic of Panama, February 22, 1985]

DEPARTMENT OF STATE
Division of Language Services
(Translation)

LS NO. 115474-A
Emb/JRP
Spanish

[Text of Government of Panama note D.M. No. 34 from Foreign Minister Cardoze to Ambassador Briggs]

Mr. Ambassador:

I have the honor to refer to Article 15(2) of the Agreement in Implementation of Article III and to Article 16(2) of the Agreement in Implementation of Article IV of the Panama Canal Treaty of 1977.

I have consulted with Drs. Romulo Escobar Bethancourt, Aristides Royo, Adolfo Ahumada, and Jaime Arias Calderon, Panamanian negotiators of those agreements, and they have confirmed to me that the provisions referred to above were discussed, negotiated, and drafted exclusively with respect to the tax exemptions that the Republic of Panama would grant to United States-citizen employees of the Panama Canal Commission and their dependents and to members of the United States Armed Forces and the civilian component and their dependents. The aforementioned provisions resulted from negotiations which did not deal with the United States authority to tax the individuals mentioned therein.

The foregoing expresses the scope of the aforementioned provisions and also represents the interpretation of this Ministry.

Accept, Mr. Ambassador, the assurances of my highest consideration and personal esteem.

[s] Fernando Cardoze Fabrega
Minister of Foreign Relations

LS NO. 115474-B

[Text of Foreign Minister Cardoze's identical notes to Panamanian negotiators Adolfo Ahumada, Romulo Escobar Bethancourt, and James A. Arias]

In your capacity as negotiator of the Panama Canal Treaty, I should like to have your opinion on the correct interpretation of Article 15(2) of the Agreement in Implementation of Article III and Article 16(2) of the Agreement in Implementation of Article IV. Especially, there is an interest in determining whether the tax exemptions referred to in the aforementioned provisions, which are granted to United States-citizen employees of the Commission and their dependents and to employees of the United States Armed Forces and the civilian component and their dependents, refer to tax exemptions from both the Republic of Panama and the United States of America.

I avail myself of this opportunity to renew to you the assurances of my distinguished consideration and esteem.

LS No. 115474-C

[Text of Dr. Ahumada's February 21 reply]

Regarding your consultation of February 20, I am happy to confirm that Article 15(2) of the Agreement in Implementation of Article III and Article 16(2) of the Agreement in Implementation of Article IV of the Panama Canal Treaty of 1977 were discussed, negotiated, and drafted exclusively with respect to the tax exemptions that the Republic of Panama would grant to United States-citizen employees of the Commission and their dependents and to members of the United States Armed Forces and the civilian component and their dependents. The aforementioned provisions resulted from negotiations that did not deal with the United States authority to tax the individuals mentioned therein.

Accept, Mr. Minister, my high consideration.

LS No. 115474-D

[Text of Dr. Escobar's February 22 reply]

Regarding your consultation of February 20, I am happy to confirm that Article 15(2) of the Agreement in Implementation of Article III and Article 16(2) of the Agreement in Implementation of Article IV of the Panama Canal Treaty of 1977 were discussed, negotiated, and drafted exclusively with respect to the tax exemptions that the Republic of Panama would grant to United States-citizen employees of the Commission and their dependents and to members of the United States Armed Forces and the civilian component and their dependents. The aforementioned provisions resulted from negotiations that did not deal with the authority of the United States of America to tax the individuals mentioned therein.

Accept, Mr. Minister, my high consideration.

LS No. 115474-E

[Text of Jaime Arias' February 22 reply]

Regarding your consultation of February 21 and based on my participation in the negotiation and drafting of the Agreement in Implementation of Article IV of the Panama Canal Treaty of 1977, I am happy to confirm to you that Article 16(2) of the Agreement, in whose drafting I took part, and, in my opinion, Article 15(2) of the Agreement in Implementation of Article III of the Treaty, were discussed, negotiated, and drafted exclusively with respect to the tax exemptions that the Republic of Panama would grant to United States-citizen employees of the Commission and their dependents and to members of the United States Armed Forces and the civilian component and their dependents. The aforementioned provisions resulted from negotiations which did not deal with the United States authority to tax the individuals mentioned therein.

Accept, Mr. Minister, my high consideration.

CERTIFICATION OF TRANSLATION

I hereby certify that the above translation bearing LS No. 115474A-E was prepared by the Division of Language Services of the Department of State and that it is a correct translation to the best of my knowledge and belief.

Dated: February 27, 1985

Jorge R. Perez
JORGE R. PEREZ
Assistant Chief, Translating Branch

APPENDIX C

Panama Canal Treaties: Hearings before the Senate Comm. on Foreign Relations, 95th Cong., 1st Sess. Pt. 1, at 268-269 (1977)

EXEMPTION FROM PANAMANIAN TAXES

Senator STONE. Mr. Chairman, I will be brief. We are at the end of the allotted time. This question is addressed to Mr. Hansell. In your statement you refer to exemption from Panamanian taxes. Would you read from the appropriate agreement the appropriate phrase that you refer to in your statement?

Mr. HANSELL. There are several provisions. I am not sure whether they are in the treaties or in the Implementing Agreements. Let me see if I can find these. This is from the Implementing Agreements. Do you have a set of the Implementing Agreements, Senator?

Senator STONE. I just have the treaties. I don't have the agreements.

Mr. HANSELL. Article XV of the agreement in implementation of article III of the Panama Canal Treaty, and we can give you a set of these—

Senator STONE. I think it was article XV, section 1 that raised an interesting question. I will read it to you. "By virtue of this agreement the Commission, its contractors and subcontractors are exempt from payment in the Republic of Panama of all taxes, fees, or other charges on their activities or properties." Then, in No. 2, referring to U.S. citizen employees and dependents, it says, "shall be exempt from any taxes,

fees, or other charges on income received as a result of their work for the Commission. Similarly, they shall be exempt from payments of taxes, fees, or other charges on income derived from sources outside the Republic of Panama."

Of course, when that was announced, the press reported the glee of the Zonians that they were now exempt from U.S. income tax. When Senator Glenn asked you, are there any words that you would like to see in the treaty, I was just asking myself would you like to see the words, United States, in there somewhere?

Mr. HANSELL. I am sorry to be a source of disappointment for the Panamanians, but obviously we are not entering into an agreement between the United States and Panama that would exempt U.S. citizens from U.S. tax. The purpose of this, of course, was to exempt them from Panamanian tax.

Senator STONE. How would you clarify that in words of writing?

Mr. HANSELL. I believe that is actually under way by the authorities in Panama. The Army, I think, is preparing some information for the zone residents on all aspects of this, including the tax aspect.

Senator STONE. Wouldn't you think that we could put in the understanding that I suggested to you, the clarification of our interpretation which then, when ratified by the Congress, by the Senate, and deposited, would clarify that in a little more formal way than simple advices, since you don't want to put words back in the treaty through negotiation?

Mr. HANSELL. The one comment I would have with respect to that, and this relates to a couple

of other points, is that we are dealing now with an internal U.S. matter, not a matter between the United States and Panama. That is, we don't agree with Panama how we are going to tax our citizens. That is obviously an internal matter. I would hope we could find ways of dealing with internal matters other than as understandings.

Senator STONE. You understand that if the Zonians want to try to exert their exemption from U.S. taxes that you will be in for some lawsuits. I just wanted to figure out a way to avoid that.

Mr. HANSELL. That would not be a lawsuit that I would want to undertake on their behalf, but we will find a way to avoid this.

Senator STONE. You would not undertake this on a contingency basis then? That is really not much of a lawsuit. Thank you, gentlemen.

Senator PELL. The committee will recess until 2 o'clock this afternoon.

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